National Cooperative Business Association ■ www.ncba.coop

August 5, 2009

The Honorable John D. Rockefeller
United States Senate
Committee on Commerce, Science and Transportation
Washington, DC 20510-6125

Dear Senator Rockefeller:

As the national organization representing cooperatives, the National Cooperative Business Association (NCBA) appreciates your interest in finding out more about cooperatives and their potential role in providing health care to our nation.

Cooperatives are member owned and controlled businesses that provide both social and economic benefits to the members – the people who use the services of the cooperative. Earnings are based on the member's use of the cooperative, not how much the member invests in the cooperative. The cooperative business model is an alternative to the investor owned or publicly traded form of business. Rather than having to account to outside shareholders, cooperatives respond to their members, who each have one vote, regardless of the amount of business they do with the cooperative.

NCBA represents all types of cooperatives operating in different sectors of the economy. Each sector may include cooperatives with different structures and functions. A few facts about the regulation of cooperatives:

- Cooperatives as businesses are regulated at the state level, as are most incorporated businesses, e.g, incorporation, licensing, etc.

- Depending on the sector or type of cooperative, the cooperative may be subject to state and federal regulation specific to the sector. For example, health care cooperative HMOs may be regulated by the state department of insurance, and/or the state department of health and human services, and/or state department of commerce. Credit unions are regulated by the National Credit Union Administration.

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- Cooperatives distinguish themselves from other forms of business in the way their earnings are distributed and taxed. Earnings of cooperatives typically are allocated to members, and members are taxed on those earnings. If the cooperative decides not to allocate to members, the cooperative itself is taxed on those earnings. Cooperatives generally file under subchapter T of the IRS Code, or Section 521 (agriculture cooperatives).

- Cooperatives can also be nonprofit, tax-exempt businesses; and in that case, they are treated similarly to other tax-exempt entities. There are several provisions in Section 501(c) of the IRS Code that address cooperatives operating in different sectors. These cooperatives typically return earnings to their members in the form of lower prices or enhanced services.

In response to your request for answers to questions related to cooperatives in general, and health-care cooperatives in particular, we provide the following responses:

1. What is the formal definition of a cooperative? In what sectors of the economy do cooperatives generally operate? Are cooperatives more successful as a model in certain sectors of the economy over others?

What is the formal definition of a cooperative?

Cooperatives around the world generally use the definition included in the International Cooperative Alliance (ICA) Statement on the Cooperative Identity:

"A cooperative is an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly owned and democratically controlled enterprise."

Most cooperatives fall into these four categories:

- ***Consumer-owned cooperatives***: These are cooperatives owned by their customers, such as credit unions and rural electric cooperatives.
- ***Purchasing cooperatives***: These allow individuals or businesses to essentially join together to buy goods and services in bulk, thus getting better deals. Most hospitals buy equipment together in these cooperatives.
- ***Worker-owned cooperatives***: The workers are the owners of these cooperatives. Several currently operate in home health care.
- ***Producer cooperatives***: These are farmer owned cooperatives like Land O' Lakes.

In what sectors of the economy do cooperatives generally operate?

Again, according to the ICA, the cooperative business model can be applied to any business activity. They exist in traditional economic sectors such as agriculture, fisheries, consumer and financial services, housing and production. Cooperative activity also spans to other sectors and activities including car sharing, child care, health and social care, funeral, orchestras and philharmonics, schools, sports, tourism, utilities (electricity, water, gas, etc.) and transport (taxis, buses, etc).

Are cooperatives more successful as a model in certain sectors of the economy over others?

The cooperative business model can be applied to any business activity. In the United States, cooperatives can be found in many sectors of the economy. The University of Wisconsin Center for Cooperatives, in its recently funded USDA study on the Economic Impact of Cooperatives on the US Economy, categorized cooperatives operating in the following sectors:

1. Commercial sales and marketing: farm supply and marketing, biofuels, grocery, and consumer goods retail, arts, crafts, and entertainment.
2. Social and public services: housing, health care, daycare, transportation, and education.
3. Financial services: credit unions, farm credit, and mutual insurance.
4. Utilities: electric; telephone, and water.

Most cooperatives, in the four sectors listed above, can be considered either "producer" or "consumer" cooperatives. A producer cooperative transforms member inputs into a marketable output; while a consumer cooperative purchases wholesale goods to sell to its members. Additionally, there are "purchasing" (or business-to-business) and "worker" cooperatives that operate in a wide variety of economic sectors. Purchasing cooperatives are composed of businesses that collectively buy supplies that members use in their respective businesses. Often the businesses are retail stores that collectively purchase wholesale goods to try to establish better terms of trade. A worker cooperative can be viewed as a type of producer cooperative where the input provided by members is labor.

Nearly 30,000 U.S. cooperatives operate at 73,000 places of business throughout the U.S. These cooperatives own greater than $3 trillion in assets, generate greater than $500 billion in revenue, and greater than $25 billion in wages. These and other data were used to estimate the indirect and induced impact of cooperative business activity. The study estimates that cooperatives account for nearly $654 billion in revenue, more than 2 million jobs, $75 billion in wages and benefits paid, and a total of $133.5 billion in value-added income.

Cooperatives have a significant impact in four sectors of the US economy:

Agriculture and Food. Cooperative firms account for a significant portion of economic activity in U.S. agricultural and food markets, both as providers of key inputs, and as marketing and processing agents for farm output. **According to USDA statistics, marketing and input supply cooperatives account for about a third of both total farm sector revenue and input purchases.**

Cooperatives play a key role in agricultural markets not only because they account for a significant fraction of economic activity in this sector, but also because they are believed to generate a pro-competitive effect in imperfectly competitive markets.

Cooperatives play other socially beneficial roles in the agricultural sector. They provide an opportunity for farmers to share risk and to control managerial decision making for their direct benefit. Some agricultural cooperatives are household names – Sunkist, Ocean Spray, and Organic Valley – for example, have created national recognition with their branded products. These firms provide processing and marketing services to farmers, and also the necessary logistical support to aggregate farm supply.

Data was collected from 2,535 farmer cooperatives. Collectively, these firms account for greater than $40 billion in assets, nearly $120 billion in sales revenue, and pay greater than $6 billion in wages. There are approximately 2.5 million farmer memberships and 150,000 employees. From extrapolating to the entire population (2,547 firms) and adding indirect and induced impacts to this activity, agricultural cooperatives account for nearly $130 billion in revenue, greater than 200,000 jobs, $8.9 billion in wages paid, and greater than $10 billion in valued-added income.

Credit Unions. **Credit unions play an important role in consumer banking by offering financial services to nearly one-third of all Americans, with 86.8 million memberships.** Credit unions account for 10% of the total assets of all depository institution assets. Roughly 75% of credit unions have total assets less than $100 million, while 80% of commercial banks and 85% savings institutions have assets greater than $100 million. Less than 2% of credit unions have assets greater than $1 billion. Credit unions, like commercial banks and thrifts, can be either federally or state chartered. There are currently 5,036 federally-chartered credit unions (FCUs) holding $418 billion in assets, and 3,157 state-chartered credit unions (SCCUs) holding $336 billion in assets.

Like all other financial depository institutions, credit unions take deposits and offer loans to its consumer base. While credit unions resemble banks, they have several distinctive legal differences: they are not-for-profit cooperatives with an IRS tax exemption status; they

return earnings to their membership in the form of reduced fee (interest) on loans and increased interest (dividends) on deposits; or they may re-invest earnings into the credit union.

The 8,334 credit unions account for $761 billion in assets and $40 billion in revenue, and pay greater than $9 billion in wages. There are 86.8 million credit union memberships and 237,000 employees. When indirect and induced impacts are added to this activity, credit unions account for close to $75 billion in revenue, close to 500,000 jobs, $20 billion in wages paid, and greater than $42 billion in valued-added income.

Mutual Insurance. The U.S. had 2,723 mutual property casualty insurance companies in 2007, with $1.3 trillion in cash and invested assets. The cash and invested assets of the 1,190 life and health insurance companies was more than twice that amount, at $3 trillion. Many of these companies are part of larger financial institutions.

In the mutual insurance sector, there are greater than $840 billion in assets, $140 billion in sales revenue, and nearly $2 billion in wages and benefits pay. **There are approximately 233 million memberships and 122,000 employees.** Adding direct and indirect impacts to this activity, mutual insurers account for greater than $227 billion in revenue, more than 500,000 jobs, $27 billion in wages paid, and more than $48 billion in valued-added income.

Rural Electric Cooperatives. Rural electric cooperatives are consumer-owned utilities that were established to provide reliable and affordable electricity by purchasing electric power at wholesale prices, and delivering it directly to the consumer. These distribution cooperatives are primarily located in rural areas where the return on expensive infrastructure investment apparently was not high enough to attract the investor-owned utilities. To assure an adequate supply of the cost-effective, reliable power that is vital to their survival, distribution cooperatives formed generation and transmission (G&T) cooperatives to pool their purchasing power for wholesale electricity. The G&T cooperatives provide wholesale power to their member-owners either by purchasing and delivering power from public or investor-owned power plants, or by generating electricity themselves.

There are 864 distribution cooperatives delivering 10% of the nation's total kilowatt hours electricity to ultimate consumers each year. **Rural electric cooperatives serve 12% of the nation's electric consumers (42 million people), but own and maintain 42% of the nation's electric distribution lines that cover 75% of the country's land mass.** Although electric cooperatives are not the dominant providers of electricity nationwide, they are the primary providers in most of the country's rural areas. Currently, 66 G&T cooperatives own 6% of the nation's miles of transmission lines. Forty-five own generation facilities that account for approximately 5% of the total electricity generated in the U.S.

There are 911 electric utilities, and collectively these firms account for greater than $97 billion in assets, exceed $34 billion in sales revenue, and pay close to $4 billion in wages. There are approximately 16 million memberships and 67,000 employees. By extrapolating to the entire population (929 firms) and adding indirect and induced impacts to this activity, electric cooperatives account for greater than $45 billion in revenue, nearly 130,000 jobs, $6.6 billion in wages paid, and greater than $11 billion in valued-added income.

2. What is the history of health-related cooperatives in America? Is the mutual insurance model upon which consumer health-care cooperatives are based still a widely-used model for health insurance today? Is this a model that has grown or decreased since health-care cooperatives were first created?

What is the history of health-related cooperatives in America?

According to the University of Wisconsin study, cooperatives have been part of the U.S. health-care system since the early 1900s, when hospitals formed the earliest purchasing groups. These purchasing organizations that still operate are organized as nonprofits or cooperatives, serving local, regional, and/or national markets. Although joint purchasing by hospitals is still the most active sub-sector within health care, organizations and individuals cooperate to achieve a wide range of health-related goals:

- Hospitals and clinics save money by engaging in joint purchasing or service delivery.
- Employer groups jointly negotiate better choices in health insurance rates for their employees.
- Cooperatives/collectives offer controlled access to medical marijuana.
- Worker-owned homecare cooperatives strive to improve service to clients through better working conditions for their workers.
- Provider networks cooperate to improve rural health care.

The first group purchasing organization in health care was formed in 1910 to purchase laundry services in New York. These organizations negotiate with vendors for a wide range of hospital supplies and services. In the 1970s and 1980s, rural areas in the U.S. were losing their doctors, hospitals, and clinics. Rural health-care providers responded by forming health networks. Some early networks were organized as cooperatives, but most are nonprofits with boards that include a large percentage of network members. Networks may offer their members administrative services.

Beginning in the late 1920s, studies urged the adoption of pre-paid and group practice medicine. This recommendation was met with strong opposition. As a result, the first health cooperative, the Community Health Plan of Elk City Oklahoma, was organized in 1929. Three large pioneer consumer cooperative health plans, Group Health Cooperatives of Puget Sound, St. Paul, and Washington DC, soon followed. Similar cooperatives were organized in New Jersey, Texas, California, New York and Wisconsin. Today, five remain: Group Health Cooperative of Washington, HealthPartners, Group Health Cooperative of Eau Claire, First Plan, and Group Health Cooperative of Southern Wisconsin. They have a collective membership of over two million people.

During the 1970s, in response to rising health insurance costs, employers began to form groups to purchase health insurance. Many purchasing groups were cooperatives. More than 25 states have statutes that promote state or employer-sponsored purchasing cooperatives. Much of the legislation was in place by the early 1990s, although some legislative activity continues. Many policy makers and communities hoped that the cooperatives would achieve significant cost savings, but analysts recognized the difficulty of avoiding adverse selection without some type of mandated use. For example, in Texas, legislation was passed in 1993, 2003, and 2005 that authorized groups of employers to form cooperatives to purchase health insurance. The cooperatives were required to form as nonprofits, and then register as purchasing cooperatives with the Texas Department of Insurance.

Worker-owned home-care cooperatives are emerging as a way to both address high staff turnover, and to improve the quality of home-care services provided to the elderly and disabled. The first worker-owned home-care cooperative, Cooperative Home Care Associates (CCHA), was formed in New York City in 1985, as an alternative to nonprofit and private agencies. CCHA's goal was to reduce turnover and provide quality home care to clients by improving the work place and compensation for home-care paraprofessionals. Since 1985, a small number of additional worker-owned home-care cooperatives have been formed.

Is the mutual insurance model upon which consumer health-care cooperatives are based still a widely used model for health insurance today?

No. The existing consumer-owned health-care cooperatives in Washington, Minnesota, and Wisconsin are based on the prepaid HMO model of providing health care. It is our understanding, from the National Association of Mutual Insurance Companies (NAMIC), that most mutual insurance companies provide life and casualty insurance. NAMIC also reports that while some mutual insurance companies may sell health insurance, it is rare that a mutual insurance company will underwrite health insurance.

Is this a model that has grown or decreased since health-care cooperatives were first created?

The five existing consumer-owned health-care cooperatives have grown, in number of members and size of the business, over the past few decades. But the overall number of consumer-owned health-care cooperatives has decreased.

Health insurance purchasing cooperatives, worker cooperatives providing health-care services, and hospital supply purchasing cooperatives have increased over the past decade. The University of Wisconsin data from 192 health-care cooperatives indicates that collectively these firms account for greater than $1billion in assets, greater than $3 billion in sales revenue, and pay $283 million in wages. There are approximately 961,000 memberships and 73,000 employees. By extrapolating to the entire population (305 firms) and adding indirect and induced impacts to this activity, health-care cooperatives account for greater than $5 billion in revenue, close to 500,000 jobs, $1billion in wages paid, and greater than $1billion in valued-added income.

3. What are the different types of health-related cooperatives in existence today? How many cooperatives are currently operational in the U.S. within each of these categories (please provide the names and geographic locations of each of these cooperatives)? Are consumer health-care cooperatives currently available, or have they historically been available, in all areas of the country?

As previously noted, health-care cooperatives fall into three categories: consumer owned, worker owned, and group purchasing owned by businesses or hospitals.

Today consumer health-care cooperatives are only available in the Northwest: Washington, Oregon, the upper Midwest Minnesota, and Wisconsin.

At the height of the consumer-owned health-care cooperatives, availability included the following states: California, Washington, New Jersey, New York, Minnesota, Wisconsin, and Texas.

4. How many Americans are enrolled in consumer health-care cooperatives?

Approximately 2 million consumers are member owners of consumer-owned health-care cooperatives.

5. How many health-related cooperatives (in all categories) have ceased to exist in the last thirty years? What are some common features of health-related cooperatives that have failed to succeed? When consumer health-care cooperatives fail, what happens to the consumers who are enrolled in them?

Easily accessible data and information on the number of health-related cooperatives that have ceased to exist over the past 30 years does not exist. Approximately 10 consumer-owned health-care cooperatives have merged with other cooperatives, or have been purchased by other nonprofit or for-profit health-care providers. Over the same period, the number of worker and purchasing cooperatives providing health care has increased.

What are some of the common features of health-related cooperatives that have failed to succeed?

There is no study that has documented the numbers, nor the reasons for past failures in health-care cooperatives in the U.S. However, years of study of the cooperative movement, and its better documented sectors, have shown that in order to be successful, any cooperative business must have positive conditions and performance in the following four areas:

(1) Strong business and financial performance, including sound capitalization and attainment of significant scale.
(2) Membership participation and governance though a democratically controlled and actively engaged Board of Directors.
(3) Involvement of cooperative apex bodies that provide industry-wide support for a cooperatives sector.
(4) Favorable general business environment conditions.

Whether it is in the health care or other sectors, a cooperative that is not well suited with respect to each of these four areas, has reduced prospects for success. From our own recent experience in the United States, insufficient scale, inadequate capitalization, and disconnected memberships have been the principle challenge to cooperative success.

When consumer health-care cooperatives fail, what happens to the consumers who are enrolled in them?

It is our understanding that most health-care cooperatives that failed have been merged with, or sold to, other health-care organizations. In those cases, the members are blended into the new company and continue to receive services.

6. Why have health-related cooperatives such as Group Health of Washington and HealthPartners of Minneapolis succeeded while other cooperatives, such as Group Health Association in Washington, DC and PacAdvantage of California failed?

Any response would be speculative, but both "successes" are subject to the state regulatory, health, and economic environment in which they operate. The success of Group Health and HealthPartners can be attributed to the timing of their entrance into the market, the health-care environment in which they work, and some of the innovative steps they have taken in their approach to delivering health-care services.

In an interview with our publication, Cooperative Business Journal, HealthPartners CEO Mary Brainerd attributed their success in part to the focus on the consumer perspective. In addition, she pointed out the unique environment in Minnesota where group-health insurance is sold through nonprofits, their higher income levels for subsidies, and the small group market which is very active. She also mentioned that HealthPartners implemented the electronic medical records system before other health organizations.

With regard to why the other entities failed, we have not been able to find case studies or speak with any of the members of those cooperatives.

7. What is the current state and/or federal regulatory structure for health-related cooperatives? Are there standard licensure requirements? Are there standard requirements for board structure and membership? What are the requirements for solvency?

The state and/or federal regulatory structure for health-related cooperatives is the same as for any other type of health-care organization. It depends on the type of health-related cooperative that is at issue. If it is a home-care cooperative, it would be subject to rules for home-care organizations. For those consumer-owned, integrated health systems like Group Health, they are regulated as HMOs, subject to the Department of Insurance, Department of Health, and the Department of Corporations Oversight.

With regard to corporate licensing, governance, and membership, cooperatives would be subject to the state general cooperative, sector specific cooperative or corporation law. If the cooperative is incorporated as a nonprofit, it would have to comply with state rules for nonprofits, including those addressing insolvency. The solvency requirements may also be included in general or sector specific cooperative laws, but, as previously stated, it depends on the sector. For example, credit unions would obviously be subject to the Federal National Credit Union Administration solvency requirements. Mutual insurance companies would be subject to state insurance solvency requirements.

NCBA is not able to fully respond to some of these questions because there is no information available on the particular subject. We understand that there may be some frustration over not having information and data on cooperatives. For years, we have worked to address this research gap and recently secured funds through Congressional appropriations to study the economic impact of cooperatives on the national economy. However, this initial research did not delve into the history or the impact of the health-care cooperative sector.

The results of the first phase of the USDA-funded research by the University of Wisconsin Center for Cooperatives were published in April 2009. This represents the first time there has been data on the size, scope, and impact of the sectors. We now know that there are nearly 30,000 cooperative businesses operating in every sector of the economy. But there still needs to be more research to assess their role and impact in different sectors of the economy.

Thank you for the opportunity to respond to your questions. Please feel free to call me if you need further assistance.

Sincerely,

Paul Hazen

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President and CEO

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